69

No. 06-1210

FILED
OCT 9 - 2007
OFFICE OF THE CLERK
SUPREME COURT, U.S.

IN THE

Supreme Court of the United States

GENERAL ELECTRIC COMPANY,
Petitioner,

v.

COMMISSIONER, NEW HAMPSHIRE
DEPARTMENT OF REVENUE ADMINISTRATION,
Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of New Hampshire

PETITIONER'S SUPPLEMENTAL BRIEF IN REPLY TO BRIEF FOR THE UNITED STATES AS AMICUS CURIAE

CARTER G. PHILLIPS
SIDLEY AUSTIN LLP
1501 K STREET, NW
WASHINGTON, DC 20005
(202) 736-8000

WALTER HELLERSTEIN*
JEROME B. LIBIN
MARY E. MONAHAN
SUTHERLAND ASBILL
& BRENNAN LLP
1275 PENNSYLVANIA AVE., NW
WASHINGTON, DC 20004
(202) 383-0100

BOBBY L. BURGNER
FRANK YANOVER
JOHN AMATO
GENERAL ELECTRIC
COMPANY
3135 EASTON TURNPIKE
FAIRFIELD, CT 06828
(203) 373-2501

WILLIAM F.J. ARDINGER
RATH, YOUNG AND
PIGNATELLI, P.C.
ONE CAPITAL PLAZA
CONCORD, NH 03302
(603) 226-2600

Counsel for Petitioner

October 9, 2007

*Counsel of Record

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20002

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES ii

I. AN "AGGREGATE" STANDARD FOR DETERMINING DISCRIMINATION IS NOT APPROPRIATE IN THIS CASE 2

II. NEW HAMPSHIRE'S TAXING SCHEME DISCRIMINATES AGAINST GE EVEN UNDER THE "AGGREGATE" APPROACH OF THE UNITED STATES 5

III. THE DECISION BELOW CONFLICTS WITH *FULTON*, *BOSTON STOCK EXCHANGE*, AND THEIR STATE COURT PROGENY 8

IV. THE "OTHER FACTORS" IDENTIFIED BY THE UNITED STATES DO NOT COUNSEL AGAINST PLENARY REVIEW 10

CONCLUSION 10

TABLE OF AUTHORITIES

Page

CASES

American Trucking Assns, Inc. v. *Michigan Pub. Serv. Comm'n*, 545 U.S. 429 (2005) 6-7

American Trucking Assns, Inc. v. *Scheiner*, 483 U.S. 266 (1987) 6

Barclays Bank PLC v. *Franchise Tax Bd.*, 512 U.S. 298 (1994). 5

Boston Stock Exchange v. *State Tax Comm'n*, 429 U.S. 318 (1977) 8-9

D.D.I., Inc. v. State, 657 N.W.2d 228 (N.D. 2003). 7, 9

Farmer Bros. Co. v. Franchise Tax Bd., 134 Cal. Rptr. 2d 390, 400 (Cal. App. 2003), *cert. denied*, 540 U.S. 1178 (2004). 7

Fulton Corp. v. *Faulkner*, 516 U.S. 325 (1996) 8

General Motors Corp. v. Franchise Tax Bd., 16 Cal. *Rptr.* 3d 41, 57 (Cal. App. 2004), *aff'd in part and rev'd in part on other grounds*, 139 P.3d 1183 (Cal. 2006) 7

Japan Line, Ltd. v. *County of Los Angeles*, 441 U.S. 434 (1979) 7

Kraft Gen. Foods, Inc. v. *Iowa Dep't of Rev. & Finance*, 505 U.S. 71 (1992) 3-5, 7

Mobil Oil Corp. v. Commissioner of Taxes, 445 U.S. 425 (1980) 4

CONSTITUTION, STATUTES AND RULES

United States Constitution, Art. I, sec. 8, cl. 3 ..... 1, 7

N.H. Admin. Rule Rev. 307.07(g) 5

N.H. Admin. Rule Rev. 307.07(j) 5

The facial discrimination against foreign commerce in this case is stark: New Hampshire grants a tax deduction for dividends received from foreign subsidiaries *if, and only if,* those foreign subsidiaries conduct income-producing activity in New Hampshire. Consequently, the regime on its face favors the investment in foreign corporations that conduct in-state rather than out-of-state activity, in violation of settled Commerce Clause principles.

The United States is unperturbed by this discrimination because it purportedly "focuses on only half of the relevant question." U.S. Br. 8. According to the United States, there is no discrimination when one looks at "New Hampshire's taxing regime as a whole and ... the aggregate tax imposed upon a unitary business." *Id.* (quoting Pet. App. 17a). In other words, if one looks at the tax imposed on the foreign subsidiary *as well as* the tax imposed on the recipient of the foreign subsidiary's dividend, one cannot demonstrate discrimination because the "discriminatory tax benefit" (*id.*) conferred on the dividend recipient (the dividends received deduction) is "fully matched by a corresponding burden" (*id.*) on the foreign subsidiary (the tax).

But it is the United States, not GE, that is being myopic here. By ignoring the fact that other jurisdictions (like New Hampshire) impose taxes on the foreign subsidiary wherever it operates, New Hampshire creates a tax-induced incentive for New Hampshire dividend recipients to locate their dividend-paying subsidiaries within the State in order to avoid a second layer of tax on the dividends. Locating the subsidiary in any other jurisdiction would subject the subsidiary's operating income to tax where it operates and its dividends to a tax in New Hampshire. For that reason, every court that has considered a regime similar to New Hampshire's has found that it violates the Commerce Clause bar against discriminatory taxes, thereby precipitating a clear conflict with the decision below.

The source of the United States' myopia in this case is its failure to distinguish clearly between the separate company reporting regime at issue here and the purportedly "analogous" (U.S. Br. 13 n. 6) combined reporting regimes in cases on which it relies for its "aggregate" approach to the question presented. Moreover, even taken on its own terms, the United States' "aggregate" approach cannot mask the discrimination that underlies this case and its incompatibility with this Court's precedents and those of every state court that has considered the precise issue presented here. At the very least, it is incumbent upon this Court to resolve this conflict and to clear up the confusion and continuing controversy over the meaning of footnote 23 in *Kraft*, whose proper interpretation lies at the heart of this case.

I. AN "AGGREGATE" STANDARD FOR DETERMINING DISCRIMINATION IS NOT APPROPRIATE IN THIS CASE

The United States' brief in support of the "aggregate" standard for analyzing the discrimination at issue in this case rests squarely on a false analogy between the combined reporting regime that New Hampshire requires for domestic members of a unitary group and the separate reporting regime that New Hampshire requires for foreign subsidiaries.

Under a combined reporting regime, income of the group members is combined on a single return; intercompany transactions among group members (such as dividend payments) are disregarded; and the resulting income is apportioned to the taxing State. See Pet. 4. Under a separate reporting regime, by contrast, no income is combined. Each company files its own return; transactions between companies (such as dividend payments) are respected; and each company's income is separately apportioned to the taxing State. See Pet. 7. When a company filing under a separate reporting regime pays a dividend to a

company filing under a combined reporting regime, the separate reporting rules apply to the payment, even though all the companies involved may be engaged in a unitary business. Although such dividends would be disregarded if all the companies joined in a combined report, they are respected because "they constitute income to the ... combined group." Br. Opp. 8.

GE maintains that the proper analysis of the discrimination issue in this case must respect the separate company regime that New Hampshire has established for foreign subsidiaries and cannot be analyzed under an "aggregate" approach (such as that embraced by combined reporting). GE relies on the fact that this Court in *Kraft* flatly rejected the "aggregate" approach in the context of a separate reporting regime (like Iowa's there and New Hampshire's here) – by focusing on taxation of the respective dividend streams at issue without aggregating the tax liability of both the parent and the subsidiary. The United States argues, however, that "*Kraft* ... cannot plausibly be read, as GE would have it, to preclude consideration of the tax burden imposed by New Hampshire on the foreign subsidiary ...." U.S. Br. 11. The reason, according to the United States, was that "there was no 'independent basis' for taxing the foreign subsidiary in Iowa, because Iowa did not have a *unitary tax scheme*" (*id.* (emphasis supplied)), whereas "[u]nder the *unitary* approach to determination of taxable income, New Hampshire would have had an 'independent' basis for taxing ... the income of foreign subsidiaries doing no business in New Hampshire ...." *Id.* (emphasis supplied).

The foregoing statement illustrates the depth of the United States' confusion over the issues presented by the petition. First, every State *must* have a "unitary" approach to taxing income when, as in *Kraft* and this case, it seeks to include the dividends that a nondomiciliary parent (Kraft and GE) receive from their foreign subsidiaries. That is because

the constitutional predicate for a State's apportionment and taxation of the dividend income received by a nondomiciliary corporation is that the subsidiaries constitute part of the dividend recipient's "unitary" business conducted within the State. *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425, 439 (1980) ("the linchpin of apportionability in the field of state income taxation is the unitary-business principle"). Consequently, the foreign subsidiaries in *Kraft*, like GE's foreign subsidiaries in this case, necessarily were part of the dividend recipient's unitary business, because Iowa or New Hampshire would otherwise have lacked the constitutional authority to include such dividends in the tax base to begin with. See *Kraft*, 505 U.S.at 72 (Kraft operated "a *unitary* business . . . in the United States and several foreign countries") (emphasis supplied).

Second, assuming that what the United States meant to say was that there was no "independent" basis under *Kraft* for taxing the foreign subsidiary in Iowa because Iowa did not have a *combined* reporting scheme for taxing unitary affiliates but New Hampshire would have had such an "independent" basis for taxing foreign subsidiaries under its *combined* approach, the United States simply ignores the indisputable fact of this case that New Hampshire's combined approach *prohibits* the inclusion of GE's foreign subsidiaries in the group. In short, the United States' analysis is based on a total misunderstanding of New Hampshire tax law.

Third, even if, contrary to the facts, New Hampshire had applied a combined reporting approach to taxing GE's unitary foreign subsidiaries, this would not have provided an "independent" basis for taxing GE's foreign subsidiaries that do no business in the State. This Court has clearly indicated that inclusion of a corporation within a combined group of unitary affiliates does *not* establish a nexus with – and, consequently, an "independent" basis for – taxing members

of the group who have no substantial contact with the State. *Barclays Bank PLC* v. *Franchise Tax Bd.*, 512 U.S. 298, 311-12 n.10 (1994). An "independent basis" for taxation within the meaning of *Kraft* footnote 23 can be established only by the subsidiary's taxable presence in the State through the conduct of business activities there.

In short, the United States' misreading of *Kraft* provides no basis for adoption of an "aggregate" approach.[1]

II. NEW HAMPSHIRE'S TAXING SCHEME DISCRIMINATES AGAINST GE EVEN UNDER THE "AGGREGATE" APPROACH OF THE UNITED STATES

Even assuming that it were appropriate to adopt the United States' "aggregate" approach to discrimination in this case, the discrimination against GE and its foreign subsidiaries would remain. Under the United States' approach, the appropriate inquiry focuses upon "the aggregate tax imposed upon a unitary business." U.S. Br. 8 (quoting Pet. App. 17a). Under this approach, according to

---

[1] The United States suggests that all this is beside the point because GE could have avoided the discrimination inherent in New Hampshire's separate reporting regime by *electing* to file on a worldwide combined basis. U.S. Br. 12 n.5. This is simply wrong. The New Hampshire Department of Revenue Administration has promulgated rules that require the filing and signing of a "water's edge combined group" form, which automatically effect "the certification required by the statute." N.H. Admin. Rule Rev. §§ 307.07(g), 307.07(j). Accordingly, the only way a taxpayer may avoid the water's edge filing requirement is to fail to file and sign the required tax form, which is illegal. Indeed, none of the Department's tax forms or rules even suggests that there is any option or "election" to file other than the required water's edge combined return. The court below recognized this requirement when it observed that the "income of foreign members of the unitary business is excluded from the combined report if the foreign members qualify as an 'overseas business organization[].'" Pet. App. 3a.

the United States, there was no discrimination, "because there was no showing that 'the aggregate tax imposed upon a unitary business' would be higher if its foreign subsidiaries did no business in New Hampshire and lower if they did." *Id.* In other words, because New Hampshire would tax either the income earned by a unitary subsidiary doing business in New Hampshire (but not its dividends) or the dividends paid by a unitary subsidiary not doing business in New Hampshire, the two unitary businesses are in substance being treated the same.

The problem, of course, is that these two unitary businesses are *not* the same. One of the businesses has a subsidiary doing business in New Hampshire and the other does not. Just as it discriminates against interstate or foreign commerce to provide *different* (and better) *treatment* to *similarly situated* taxpayers based solely on their local activities, so it discriminates against interstate or foreign commerce to provide *similar treatment* to *differently situated* taxpayers based solely on their local activities. *See, e.g.*, *American Trucking Assns, Inc.* v. *Scheiner*, 483 U.S. 266 (1987) (invalidating flat tax applied equally to all trucks because local trucks engaged in more in-state activity, and thus paid lower per mile tax, than out-of-state trucks). Thus, New Hampshire discriminates against foreign commerce by according essentially the same tax treatment to unitary businesses that have different levels of in-state activity.

The *American Trucking* case reveals an even more fundamental flaw in the New Hampshire scheme. The Court in *American Trucking* observed that the flat tax discriminated against interstate commerce because it was not "internally consistent," *i.e.*, if hypothetically replicated by every jurisdiction it would impose a greater burden on interstate than on intrastate commerce. *American Trucking*, 483 U.S. at 282-87. As this Court more recently described "the 'internal consistency' test ... that test asks, 'What would happen if all

States did the same?'" *American Trucking Assns, Inc.* v. *Michigan Pub. Serv. Comm'n*, 545 U.S. 429, 437 (2005).

Because the protection afforded by the dormant Commerce Clause to foreign commerce "is broader than the protection afforded to interstate commerce," *Kraft*, 505 U.S. at 79; *see also Japan Line, Ltd.* v. *County of Los Angeles*, 441 U.S. 434, 449 (1979), New Hampshire's taxing regime plainly discriminates on its face against foreign commerce in violation of the internal consistency test. If every jurisdiction followed New Hampshire's lead and taxed corporations on both their operating income and their dividends, but provided a deduction for dividends reflecting income that had already been taxed in the hands of the payor, it is clear that parent-subsidiary structures involving foreign jurisdictions would bear a higher tax burden than those that confined their activities to a single State.

Indeed, the decisions of other state courts in direct conflict with the decision below have recognized that regimes indistinguishable from New Hampshire's violate the internal consistency test: As one of these courts observed, "the imposition of the dividends received deduction by every State would favor intrastate commerce over interstate commerce by giving a greater tax benefit to taxpayers investing in their home state corporations as opposed to out-of-state corporations or corporations engaged in multistate business." *Farmer Bros. Co. v. Franchise Tax Bd.*, 134 Cal. Rptr. 2d 390, 400 (Cal. App. 2003), *cert. denied*, 540 U.S. 1178 (2004). *Accord, General Motors Corp. v. Franchise Tax Bd.*, 16 Cal. Rptr. 3d 41, 57 (Cal. App. 2004), *aff'd in part and rev'd in part on other grounds*, 139 P.3d 1183 (Cal. 2006); *D.D.I., Inc. v. State*, 657 N.W.2d 228, 234 (N.D. 2003).

III. THE DECISION BELOW CONFLICTS WITH *FULTON*, *BOSTON STOCK EXCHANGE*, AND THEIR STATE COURT PROGENY

The United States' effort to distinguish *Fulton* from the instant case suffers from the same confusion that infects the rest of its brief. According to the United States, *Fulton* involved a prohibited reduction in a property tax "based on a *separate* economic actor's level of in-state activity" (U.S. Br. 15 (emphasis in original) with "no unity of business between the issuing corporation and the taxpaying stockholder, and no equalization of burdens under a single taxing statute." *Id.* The tax here is different, says the United States, because "the allegedly discriminatory tax benefit pertained to the same tax and the same economic actor (*i.e.*, the unitary business)." *Id.* at 16.

But the United States' argument stumbles on its own premise. New Hampshire's tax as applied in the separate reporting context of this case does *not* apply to the "same tax" and the "same economic actor." The tax applies to two different taxpayers (or potential taxpayers) – the dividend recipient and the dividend payor. The United States' characterization of the tax as one on "the unitary business" once again reflects its confusion over a *combined* report, which arguably determines the tax of a single economic actor, and the separate returns filed by a parent and a subsidiary, who happen to be engaged in a unitary business. The fact that a State chooses to relieve one taxpayer of liability based on the liability of another taxpayer does not render the tax as one on the "unitary business."

The United States' attempt to distinguish *Boston Stock Exchange* fails for reasons similar to those described above in connection with *Fulton*. Although this Court condemned the State's effort in *Boston Stock Exchange* to "foreclose[] tax neutral decisions" by offering a tax benefit

for local activity (429 U.S. at 331) the United States contends that GE's "decision whether to have its foreign subsidiaries do business in New Hampshire was essentially tax-neutral" U.S. Br. 17. But this statement rests on the false assumption that New Hampshire imposes a single tax on a unitary business rather than a separate tax on the parent and subsidiary. Once that false assumption is removed, the position of the United States collapses, because the benefit offered the parent for moving its subsidiary into New Hampshire is conceptually indistinguishable from the benefit offered sellers of stock to move their stock sales into New York.

Finally, the United States' contention that there is no conflict between the decision below and the decision of the North Dakota and California courts invalidating dividend received deductions (DRDs) confined to dividends reflecting income on which tax has already been paid simply blinks reality. The United States denies that there is a conflict between *D.D.I.* and the decision below because the State in *D.D.I.* conceded that the taxing scheme facially discriminated against interstate commerce, and sought to defend the scheme only on the basis that it was compensatory. 657 N.W.2d at 231. In fact, the very same compensatory tax issues that were raised in *D.D.I.* were raised below (see Brief of General Electric at 18-20; Brief of Commissioner, Department of Revenue Administration at 29; Reply Br. of General Electric at 9-10), and the decision below rejecting these claims necessarily resolved them against GE, thereby creating an irreconcilable conflict with *D.D.I.*[2]

---

[2] The United States' effort to distinguish the two cases on their facts borders on the frivolous. The difference in stock ownership requirements in the two cases is a distinction lacking constitutional significance. Pet. Rep. Br. 3. The suggestion that North Dakota could have taxed D.D.I., a nondomiciliary corporation, on dividends it received that did not constitute part of D.D.I.'s unitary business carried on in part in North

The United States does not even attempt to distinguish the California Court of Appeal cases that are irreconcilable with the decision below, but perfunctorily points to another California case involving *combined* reporting as somehow undercutting the conflict. U.S. Br. 19. As we have demonstrated at length above, the United States' effort to elide combined reporting regimes with separate company reporting regimes is a false analogy that permeates its entire brief. See also Pet. Rep. Br. 5-9.

IV. THE "OTHER FACTORS" IDENTIFIED BY THE UNITED STATES DO NOT COUNSEL AGAINST PLENARY REVIEW

The United States contends that the repeal of New Hampshire's statute and the alleged dispute over its proper interpretation counsel against review in this case. As GE has explained in its Reply to New Hampshire's Supplemental Brief in Opposition, the repeal of New Hampshire's statute has no impact New Hampshire's treatment of dividends, because the treatment is mandated by state constitutional law. For the same reason, the purported uncertainty surrounding the interpretation of the DRD statute is beside the point. New Hampshire's constitutional prohibition against double taxation of corporate income compels the treatment that GE claims is impermissibly discriminatory.

CONCLUSION

The petition for a writ of certiorari should be granted.

Dakota (U.S. Br. 18 & n.8) is contrary to all controlling constitutional authority. See *supra* pp. 4-5. The goal of avoiding double taxation of corporate income in the hands of the payor and the payee was identical in both cases. Pet. Rep. Br. 3-4.

Respectfully submitted,

CARTER G. PHILLIPS
SIDLEY AUSTIN LLP
1501 K STREET, NW
WASHINGTON, DC 20005
(202) 736-8000

WALTER HELLERSTEIN*
JEROME B. LIBIN
MARY E. MONAHAN
SUTHERLAND ASBILL
& BRENNAN LLP
1275 PENNSYLVANIA AVE., NW
WASHINGTON, DC 20004
(202) 383-0100

BOBBY L. BURGNER
FRANK YANOVER
JOHN AMATO
GENERAL ELECTRIC
COMPANY
3135 EASTON TURNPIKE
FAIRFIELD, CT 06828
(203) 373-2501

WILLIAM F.J. ARDINGER
RATH, YOUNG AND
PIGNATELLI, P.C.
ONE CAPITAL PLAZA
CONCORD, NH 03302
(603) 226-2600

Counsel for Petitioner

*Counsel of Record

October 9, 2007